No. 8665

In the United States Circuit Court of Appeals

For the Ninth Circuit.

In the Matter of

FRED E. KEELER,

a Debtor.

CLARENCE OCHS, GUY A. KELLEY and P. L. NEWCOMB,

Appellants,

vs.

O. T. GILBANK and HUGO O. ROMBERG, as Committeemen of the Estate of FRED E. KEELER, a Debtor,

Appellees.

APPELLANTS' OPENING BRIEF.

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Statement of the Pleadings and Facts Disclosing the Basis Upon Which it Is Contended That the District Court Had Jurisdiction and That the United States Circuit Court of Appeals for the Ninth Circuit Has Jurisdiction Upon Appeal to Review the Order in Question.

O. T. Gilbank and Hugo O. Romberg, the regularly elected, duly qualified and acting committee of the estate

of Fred E. Keeler, a debtor, appointed and elected pursuant to the terms of an extension proposal accepted and approved under the provisions of section 74 of chapter 8 of the Bankruptcy Act of the United States of America, filed a petition for order to show cause [R. p. 10] to the referee in bankruptcy, Honorable Hugh L. Dickson, alleging that on the 6th day of November, 1935, they entered into a certain agreement with Arthur G. Gage, annexing thereto and marked Exhibit "A" a full, true and correct copy of said agreement.

The petition further states that Arthur G. Gage had assigned said agreement and all rights accrued thereunder to Clarence Ochs, Guy A. Kelley and P. L. Newcomb, the present owners and holders of said agreement.

Petitioners (appellees) further state that the estate of Fred E. Keeler, a debtor, had never at any time owned more than a 75% interest in the oil and gas produced from the well now located upon the premises described in said contract; that in making and entering into said contract petitioners (appellees) did not believe they were contracting, nor did they intend to contract, with reference to any oil or gas produced from said well other than that owned by said estate.

The said petition for order to show cause further alleges that Clarence Ochs, Guy A. Kelley and P. L. Newcomb (appellants) claim, by virtue of said contract, that they are entitled to 60% of all oil and/or gas produced from said well, instead of and in lieu of 60% of 75% of such

oil and/or gas, and that they (appellants) have retained 60% of the total proceeds of the oil and gas derived from said well, which has necessitated petitioners (appellees) paying to the Pacific Electric Land Company and Associated Oil Company out of the 40% paid to them (petitioners) the moneys due said companies; that Clarence Ochs, Guy A. Kelley and P. L. Newcomb claim they have the right so to do by virtue of said agreement. [Exhibit "A", R. p. 12.]

Petitioners (appellees) prayed that an order be made and directed to Clarence Ochs, Guy A. Kelley and P. L. Newcomb, commanding them to appear at a time and place to be named in said order and show cause, if any they have, why they should not be required to account to petitioners (appellees) for 15% of the oil and/or gas produced by them from said well, being the difference between 60% of the total production of said well and 60% of 75% of the production of said well. [R. p. 12.]

Whereupon Honorable Hugh L. Dickson, referee in bankruptcy, made an order directed to Clarence Ochs, Guy A. Kelley and P. L. Newcomb (appellants), commanding them to appear before said referee in bankruptcy upon the 30th day of March, 1937, at the place specified therein, and to show cause, if any they have, why they should not be required to account to the committeemen of the estate of Fred E. Keeler, a debtor, for the proceeds of 15% of the oil and/or gas produced and sold by them from the well upon the land described in Exhibit "A" of the petition on file.

That thereafter, and on or about the 9th day of April, 1937, Honorable Hugh L. Dickson, referee in bankruptcy, made his order directing Clarence Ochs, Guy A. Kelley and P. L. Newcomb to account for and pay over to O. T. Gilbank and Hugo O. Romberg, as committeemen of the estate of Fred E. Keeler, a debtor, the 15% of the proceeds derived from the sale of oil and gas produced by said well and not theretofore accounted for by them to said committeemen of said estate. [R. p. 22.]

A petition was thereafter filed by Clarence Ochs, Guy A. Kelley and P. L. Newcomb (appellants) to review referee's order. [R. p. 23.]

The petition to review referee's order came on regularly to be heard before Honorable Geo. Cosgrave, District Judge, and, after argument by the respective counsel, and the case being submitted on briefs, the Court made and entered its minute order [R. p. 40], wherein the petition for review was denied and the decision of the referee confirmed. The order of the Court was entered on July 29, 1937. [R. pp. 41 and 42.]

The jurisdiction of the District Court and the jurisdiction of this Court upon appeal to review said order is authorized by virtue of *11 U. S. C. A., Sec. 47; 28 U. S. C. A., Sec 225; 11 U. S. C. A., Sec. 11, Chapter 2.*

The jurisdiction of this Court also rests upon the petition for and allowance of the appeal [R. pp. 59-65], bond for costs [R. p. 67], and assignment of errors [R. p. 61].

Statement of the Case.

Appellees, O. T. Gilbank and Hugo O. Romberg, as committeemen of the estate of the debtor, instituted these proceedings to recover 15% of the net proceeds of oil and gas produced from a well leased to appellants, Clarence Ochs, Guy A. Kelley and P. L. Newcomb. Proceedings based on contract. [R. p. 12.]

Appellees own four lots, located at Huntington Beach, California, upon which is located an oil well. [R. p. 13.]

The Pacific Electric Land Company was the prior owner of said lots. At the time the lots were deeded to the committeemen (appellees) the company reserved unto itself a one-fourth interest in any oil, gas or other hydrocarbon substances.

On November 6, 1935, the committeemen leased the premises to Arthur G. Gage. [R. p. 12.]

Mr. Gage and the committeemen, through Mr. Holoday, their agent, negotiated for six or eight months before the contract was executed. [R. p. 45.] Mr. Gage informed Mr. Gilbank that he would have to have 60% of the oil from the premises. [R. p. 46.] Mr. Gilbank then sent Mr. Gage to Mr. Hunter's office to have the contract drawn. [R. p. 46]. Mr. Hunter, as attorney for the committeemen, drew the contract. Later Mr. Gage learned that Mr. Gilbank said a poor contract had been drawn and that it was ambiguous. Thereupon Mr. Gage, in company with Mr. Holoday, went to Mr. Hunter's office, and Mr. Hunter said "it wasn't ambiguous, but meant that I (Gage) was to get 60%, the receiver was to get 15%; the Pacific Electric Land Company was to get 25%". [R. p. 46.]

Mr. Gage testified that his understanding with Mr. Gilbank was that he was to receive 60% of all oil and gas produced. Mr. Holoday also testified that Mr. Hunter said it was a 60-40 contract, and that Gage would receive 60%, the estate 40%, out of which they would have to pay 25% royalty, and have a net of 15% left.

Mr. Gage took possession and proceeded to operate the oil well. Thereafter he assigned his contract to Martin and Moore, retaining unto himself 10% of all oil and gas produced from said premises. [R. p. 53.] Martin and Moore operated the property from January 25, 1936, to some date in March, 1936. The Dehydrating Company, purchasers of the oil from Gage and his assignees, in accordance with instructions received from the committeemen, accounted to Martin and Moore for 50%, to Gage 10% and to the committeemen 40%. [R. p. 53.]

Martin and Moore assigned to appellants, who took over the lease in March, 1936. They did not produce oil from the well until late in the fall of 1936. Their first remittances were made in October, 1936, and were made on the basis of 60-40 of production. [R. p. 52.] Remittances continued to be made by appellants to the committeemen, in accordance with instructions given the Dehydrating Company by the committeemen. [R. p. 53.]

On January 15, 1937, Mr. Newcomb (one of the appellants) went to Mr. Gilbank's office. [R. p. 53.] The matter of royalties was not discussed, although Mr. Newcomb went there to pay the committeemen their share of the same, to-wit, 40%.

Mr. Gilbank told Mr. Newcomb that they (appellants) were facing some dispute as to the interpretation they placed on the contract. That was the first notice appellants had from anyone interested in the estate that there

was any difference of opinion regarding the interpretation of the contract. [R. p. 54.]

At that time Mr. Newcomb (appellant) paid Mr. Gilbank 40% from the sale of the oil. [R. p. 54.] Mr. Gilbank did not tell Mr. Newcomb the reason appellants would be attacked, or on what basis, but told him that he was perfectly satisfied with the conditions on which the oil had been operated and the performance of appellants' part of the contract. [R. p. 54.]

On March 13, 1937, Honorable Hugh L. Dickson, referee in bankruptcy, issued an order to show cause [R. pp. 18-19], directed to Ochs, Kelley and Newcomb (appellants). Prior to that time the committeemen had not discussed the contract with appellants, or demanded any additional royalties from them.

The gross receipts derived from the sale of oil were $3361. [R. p. 54.] The appellants paid out $4398. This sum included the amounts paid to the committeemen. The amount paid out was $1037 in excess of the amount received.

The preamble of the agreement, Exhibit "A" [R. p. 13], provides: "EXCEPTING therefrom an undivided one-fourth of all minerals contained in said real property, * * *," although paragraph 4 [R. p. 15] of the body of the agreement provides that appellants "shall be entitled to receive and retain sixty per cent (60%) of the net proceeds of all oil and gas produced, saved and sold from said premises".

On the 28th day of July, 1937, the District Court ordered that the petition for review be denied, and that the decision rendered by Honorable Hugh L. Dickson, referee in bankruptcy, be confirmed. [R. pp. 61-62.]

Specification of Assigned Errors Relied Upon and Reference to the Record Where Such Assignments Appear.

The assignment of errors, as they appear in the record [R. p. 61], are as follows:

1. The Court erred in making that certain order denying petition for review and confirming the order of referee, made and entered on the 28th day of July, 1937, reading as follows: [R. p. 61.]

2. The Court erred in making said order for the reason that said conclusion of law is not supported by and is contrary to the facts as established by the evidence.

3. The Court erred in making and adopting its conclusion that the findings of fact made by the Honorable Hugh L. Dickson are correct, and that his order made pursuant thereto is in accordance with the law.

4. The Court erred as a matter of law in failing and refusing to find that the parties had themselves determined their rights under said contract and placed their own interpretation thereon.

5. The Court erred as a matter of law in failing and refusing to find what the parties intended the language to mean of paragraph 2 of the contract.

6. The Court erred as a matter of law in failing and refusing to find what the parties understood the language to mean of paragraph 2 of the contract.

7. The Court erred as a matter of law in failing and refusing to find that the committeemen of the

estate of the debtor had acquiesced in the construction placed on the contract by the petitioners and their assignors.

8. The Court erred as a matter of law in failing and refusing to find that when general and specific provisions of a contract deal with the same subject-matter, the specific provisions, if inconsistent with the general provisions, are of controlling force.

9. The Court erred as a matter of law in failing and refusing to find that the committee of the estate of the debtor are estopped to maintain a position inconsistent with one in which they had acquiesced for a long period of time, and from which they had accepted benefits.

10. The Court erred as a matter of law in failing and refusing to find that the paragraph numbered 4 of said contract entitled the petitioners to receive and retain sixty per cent of the net proceeds of all oil and gas produced, saved and sold from said premises.

11. The Court erred as a matter of law in failing and refusing to find that the petitioners are entitled to sixty per cent of all the oil and gas produced, saved and sold from said premises.

12. The Court erred as a matter of law in finding and concluding that petitioners are entitled to sixty per cent of seventy-five per cent of all oil and gas produced, saved and sold from said premises.

Appellants' assignment of errors, set forth in the transcript of record and above repeated, may be embraced within one assignment of fundamental error, which, if

found to be well taken, will sustain the collateral assignments, viz.:

I.

The lower Court erred in its conclusion that twenty-five per cent of the oil had been excepted, and that the parties to the contract never contracted with reference to it, and, from such conclusion, in making its order denying petition for review of Clarence Ochs, Guy A. Kelley and P. L. Newcomb, and confirming the decision of the referee.

Propositions of Law.

Appellants submit the following propositions of law upon which the foregoing assignment is predicated:

I.

When parties to a contract have placed their own interpretation upon its terms and have acquiesced therein, it must be held that the parties have themselves determined their rights under said contract, and the Court will follow their interpretation, even though it be erroneous.

II.

Doubtful and ambiguous language employed by the maker of a contract in drafting its provisions, must be construed most strongly against such maker.

III.

The intent of the parties at the time the contract was entered into must control.

IV.

The committeemen are now estopped from raising the subject of the interpretation of the lease.

ARGUMENT.

POINT I.

When Parties to a Contract Have Placed Their Own Interpretation Upon Its Terms and Have Acquiesced Therein, it Must Be Held That the Parties Have Themselves Determined Their Rights Under Said Contract, and the Court Will Follow Their Interpretation, Even Though it Be Erroneous.

The Dehydrating Company that received the oil derived from the well on the premises of appellees made payment of the royalties in accordance with instructions received from the committeemen [R. p. 53], and this was on the basis of appellants receiving 50%, Gage 10%, Romberg and Gilbank, the committeemen for the estate 40%. [R. p. 53.] That was the basis upon which the parties operated in disbursing the royalties for the year 1936, and the committeemen continued to receive such royalties without protest, or making any demand on Gage or his assignees, prior to the filing of their petition for order to show cause, which occurred on the 16th day of March, 1937. [R. p. 19.] It was not denied at the hearing by the appellees that they had given instructions to the Dehydrating Company to make payment of the royalties on the basis as hereinabove set forth. They acquiesced in the construction placed on the contract by Mr. Gage and his assignees, because it was the construction agreed upon between Mr. Gage and Gilbank and Romberg. [R. p. 46.] The parties having placed their

own interpretation upon the terms of the contract and the acts of the parties done subsequent thereto in accordance with such interpretation afford one of the most reliable clues to the intention of the parties. The following cases support that principle of law:

McKell v. Chesapeake etc. R. Co., 175 Fed. 321, 99 C. C. A. 109, 20 Ann. Cas. 1097;

Webster v. Clark, 34 Fla. 637;

Mayberry v. Alhambra etc. Co., 125 Cal. at p. 446;

Mitau v. Roddan, 149 Cal. at p. 14;

Hill v. McKay, 94 Cal. p. 5, 29 Pac. 406;

Rockwell v. Light, 6 Cal. App. 563;

Keith v. Electrical Engineering Co., 136 Cal. 178;

Woodard v. Glenwood Lumber Co., 171 Cal. 513;

Preston v. Herminghaus, 211 Cal. p. 1.

POINT II.

Doubtful and Ambiguous Language Employed by the Maker of a Contract in Drafting Its Provisions Must Be Construed Most Strongly Against Such Maker.

When Mr. Gilbank and Mr. Gage agreed upon the terms of the lease [R. p. 46], Mr. Gilbank then sent Mr. Gage to Mr. Hunter's office for the purpose of having Mr. Hunter draw the contract. Mr. Hunter was the attorney for the committeemen. [R. p. 46.] When the question subsequently arose concerning the interpretation of the contract Mr. Gage, in company with Mr. Holoday, went to Mr. Hunter's office and told him that Mr. Gilbank was contending the contract should be read 60-75. [R. p. 49.] Mr. Hunter, who had drawn the lease, stated that Mr. Gilbank was "all wet"; that the contract was not ambiguous; that it meant 60% to the operator, 15% to the committeemen and 25% to the Associated Oil. [R. p. 49.] Mr. Holoday, who had formerly been the agent for the committeemen, stated that Mr. Hunter told him that the royalties under the provisions of the contract [R. p. 51] were 60-40, and that Mr. Gage would get 60% and the estate 40%, out of which they would have to pay 25% royalties, and have a net of 15% left. [R. p. 51.]

At the hearing before Honorable Hugh L. Dickson, and at the time this testimony was introduced, Mr. Hunter was present and acting as counsel for the committeemen. He heard the witnesses testify concerning his (Hunter's) interpretation of the lease, yet he (Mr. Hunter) made no denial, excepting to say that his opinion could not alter the plain provisions of the lease. The law is well settled and established that a written contract should, in case of

doubt, be interpreted against the party who has drawn it. See *section 242, 6 Ruling Case Law,* at page 854. The Court will adopt that construction of the contract which is in favor of the promisee:

> *Home of the Friendless v. Rouse,* 8 Wall. 430, 19 U. S. L. Ed. 495;
>
> *Joy v. St. Louis,* 138 U. S. 1, 11 S. Ct. 243, 34 U. S. L. Ed. 843; quoted in *German-American Mercantile Bank v. Illinois Surety Co.,* 99 Wash. p. 9, 168 Pac. 772; cited in *Torrey v. Cannon,* 171 N. C. 519, 88 S. E. 768.

We quote from section 1654 of the Civil Code of the state of California:

> "In cases of uncertainty not removed by the preceding rules, the language of a contract should be interpreted most strongly against the party who caused the uncertainty to exist. The promisor is presumed to be such party * * *."

The Court said, in *Courture v. Ocean Park Bank,* 205 Cal. 338, at page 344:

> "It is well settled that where an instrument is uncertain as to its terms it is to be construed most strongly against the party thereto who caused such uncertainty to exist."

See, also, to the same effect:

> *Payne v. Neuval,* 155 Cal. 46, 99 Pac. 476;
>
> *Union Construction Co. v. Western Union Tel. Co.,* 163 Cal. 298, 125 Pac. 242;
>
> *Bennett v. Potter,* 180 Cal. 736, 183 Pac. 156.

POINT III.

The Intent of the Parties at the Time the Contract Was Entered Into Must Control.

Section 1859 of the Code of Civil Procedure provides:

> "* * * and in the construction of the instrument the intention of the parties is to be pursued, if possible; and when a general and a particular provision are inconsistent, the latter is paramount to the former. So a particular intent will control a general one that is inconsistent with it."

In the *Reedy v. Smith,* 42 Cal. 245, case it is said that the object of a contract is to ascertain the intention of the parties in entering into it.

The Court said, in the case of *Gardner v. California Guarantee Investment Co.,* 137 Cal. 71, at page 75:

> "Hence, while the contract remains in force, and not barred by the statute, there can be no bar to the proof of the real intention of the parties or to the reformation of the contract."

In the case of *Tennant v. Wilde,* 98 Cal. App. at page 445, the Court said:

> "For the purpose of determining what the parties intended by the language used, it is competent to show not only the circumstances under which the contract was made, but also to prove that the parties intended and understood the language in the sense contended for; and for that purpose the conversation

between, and declarations of, the parties during the negotiations at and before the time of the execution of the contract may be shown. (Code Civ. Proc., secs. 1860, 1861; Atlanta v. Schmeltzer, 83 Ga. 609 (10 S. E. 543); Keller v. Webb, 125 Mass. 88 (28 Am. Rep. 209); Long v. Long, 44 Mo. App. 141; Swett v. Shumway, 102 Mass. 365 (3 Am. Rep. 471).)"

See, also:

6 *Ruling Case Law,* sec. 225, at p. 835.

Prior to the execution of the contract Mr. Gage, in discussing its provisions, told Mr. Gilbank that he could not produce the property unless he got 60% of the oil on the property. [R. p. 46.] There was a meeting of the minds on that basis as to a division of the oil produced. Whereupon Mr. Hunter drew the lease, providing for the payment to Gage of 60% of the net proceeds of all oil and gas produced, saved and sold from said premises. [R. p. 15.]

If it had not been the intention of the parties that Mr. Gage was to receive 60% of the whole it would have been a very easy matter to have stated in the lease "60% of 75% of the net proceeds of all oil and/or gas produced".

POINT IV.

The Committeemen Are Now Estopped From Raising the Subject of the Interpretation of the Lease.

We quote from 10 *Ruling Case Law,* section 22, at page 694:

> "The doctrine of equitable estoppel is frequently applied to transactions in which it is found that it would be unconscionable to permit a person to maintain a position inconsistent with one in which he has acquiesced or of which he has accepted any benefit. In order to raise an estoppel by acquiescence the party estopped must have been aware of his own rights and have perceived that the other party was acting on a mistaken notion of his rights."

The courts have held acquiescence by inaction or silence constitutes a bar.

Hoyt v. Sprague, 103 U. S. 613.

> "A person looking on and assenting to that which he has power to prevent is precluded ever afterwards from maintaining an action for damages."

Gill v. United States, 160 U. S. 426, 16 S. Ct. 322, 40 U. S. (L. Ed.) 480.

> "Acceptance of contract price for material supplied in excess of contract requirement."

Chas. Nelson Co. v. United States, 261 U. S. 17.

The committeemen accepted the benefit of the work done by Mr. Gage and his assignees in taking 300 barrels of water out of the well at great expense to Gage and his assignees, thereby enhancing the value of the property, and they are now estopped from placing a construction on the contract at variance with the construction they heretofore placed on it.

In this connection, see:

Brant v. Virginia Coal Co. etc., 93 U. S. 326;

Peoples Bank v. Manufacturers Nat. Bank, 101 U. S. 181;

Compton v. Jessup, 167 U. S. 1;

Oregon etc. R. Co. v. United States, 238 U. S. 393.

Conclusion.

Appellants therefore respectfully submit that, upon each of the points and assignment of errors, the order should be reversed.

JOHN W. CARRIGAN,

Solicitor for Appellants.